



# **CITY OF SAN DIEGO ETHICS COMMISSION AUDIT MANUAL**

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# I. INTRODUCTION

## A. Objective

San Diego Municipal Code section 26.0414 mandates that the San Diego Ethics Commission [Commission] propose procedures for conducting audits of campaign, lobbying, and conflict of interest disclosure forms. The primary objective of this manual is to set forth standards and provide guidelines and procedures to assist staff in implementing this requirement.

The *Commission* shall not audit any action or event that occurred prior to July 1, 2001, or any record thereof, whether or not that action or event was disclosed, or reasonably should have been disclosed, after that date.

## B. Audit Standards

The audit standards of the *Commission* are based on the opinions expressed in “Statement on Auditing Standards Number 7,” issued by the American Institute of Certified Public Accountants (“AICPA”). According to this statement, each audit must conform to established audit standards. AICPA auditing standards are used to measure the work done by the auditor to determine the acceptability of the audit. Auditing standards consist of general standards, standards of fieldwork, and standards of reporting. These standards are set forth in Appendix A.

## C. Definitions

Each word or phrase that is defined in this manual appears in the text of this section in italicized letters. For purposes of this manual, the following definitions shall apply:

*Audit file* includes any documents filed by a *committee*; research conducted by the auditor; correspondence between the auditor and the *committee*; and any reports arising from previous audits of the *committee*.

*Audit period* means the period of time encompassing activities by the *committee* that are covered by the audit.

*Campaign Audit Questionnaire* means a written series of questions drafted by the auditor and submitted to the *committee* prior to the *initial meeting*. This questionnaire typically contains questions seeking background information regarding the *committee*, such as the names of principals and length of time organized as a *committee*.

*Audit workpapers* means the documentation created by the auditor during the audit testing

*Auditor notification letter* means written correspondence sent by the auditor to a *committee* selected for an audit, scheduling the *initial meeting*, listing the records required for the audit, and enclosing an *audit questionnaire*.

*Ballot measure committee* means a *committee* organized to support or oppose the qualification or passage of a City measure for the ballot.

*Bank reconciliation* means a comparison of a *committee's* check register and bank statements for purposes of locating discrepancies.

*Campaign audit* means an audit of the financial activities of a *committee* organized to support or oppose a candidate or ballot measure in the City of San Diego.

*Candidate committee* means any *committee* that supports or opposes a candidate for elected office for the City of San Diego. A *candidate committee* may be a candidate-controlled committee or a committee that is not controlled by a candidate.

*City Clerk* means the duly appointed City Clerk of the City of San Diego or any authorized designee.

*Commission* means the City of San Diego Ethics Commission.

*Commission notification letter* means written correspondence sent by the *Commission* to a *committee* notifying it that it has been randomly selected for an audit.

*Committees* include *candidate committees*, and committees supporting or opposing City of San Diego ballot measures.

*Draft audit report* means a report prepared by the auditor at the conclusion of an audit, and submitted to the subject of the audit for review and comments. The *draft audit report* contains *material* findings regarding the activities of the subject of the audit.

*Final audit report* means a report prepared by the auditor at the conclusion of an audit, and either (1) contains no *material* findings; or (2) contains comments and explanations furnished by the subject of the audit in response to the *draft audit report*.

*Form 410* means the Statement of Organization form required to be filed by any entity qualifying as a recipient *committee*.

*Form 460* means the Recipient Committee Campaign Statement required to be filed by candidates, officeholders, and their controlled *committees* who have, or will, raise or spend \$1,000 during a calendar year in connection with election to officer or holding office.

*Form 461* means the Major Donor Independent Expenditure Committee Campaign Statement required to be filed by individuals or entities that make independent expenditures totaling \$1,000 or more in a calendar year to support or oppose City candidates or ballot measures.

*Form 465* means the Supplemental Independent Expenditure Report required to be filed by any *committee* making independent expenditures totaling \$1,000 or more during a calendar year to support a single candidate for local elective office or the qualification of a single ballot measure.

*Form 470* means the Officeholder and Candidate Campaign Statement (Short Form) required to be filed by officeholders and candidates who do not have a controlled *committee*, who raise less than \$1,000 in a calendar year, and who spend less than \$1,000 in a calendar year.

*Form 470 Supplement* means a report required to be filed by any officeholder or candidate who filed a Form 470 and subsequently received contributions totaling more than \$1,000 in contributions.

*Form 496* means the Late Independent Expenditure Report required to be filed by *committees* that make independent expenditures of \$1,000 or more to support a single candidate or measure during the 16 days prior to an election.

*Form 497* means the Late Contribution Report required to be filed by *committees* that make or receive contributions of \$1,000 or more during the 16 days prior to an election.

*Form 501* means the Candidate Intention Statement required to be filed by any candidate who plan to receive contributions.

*Form 700* means the Statement of Economic Interests required to be filed by any candidate for elected office in the City of San Diego.

*High Level Filer* means the Mayor, the members of the City Council, the City Attorney, City Manager, City Treasurer, City Auditor, Planning Commissioners, members of the Funds Commission, members of the Retirement Board, members of the San Diego Data Processing Corporation Board, members of the Defined Contribution Plan Board, the Ethics Commission, and any candidate for an elective office of the City.

*Initial meeting* means the first meeting between the auditor, treasurer, or representative of the *committee* selected for the audit. At this meeting, an overview of the audit process is explained, answers to the *audit questionnaire* are discussed, and internal policies and procedures of the *committee* are explained. Clarification may be sought with regard to any discrepancies the auditor may have found during the preliminary review

*Internal control* means the policies and procedures implemented by a *committee* for conducting its business

*Lobbyist* means an individual who receives or is entitled to receive the “threshold compensation” amount during any calendar quarter for lobbying, and who has had at least one direct communication with a City official in that calendar quarter. For calendar year 2002, the threshold compensation is \$2,288.

*Lobbyist audit* means a review of the financial activities of a *lobbyist* registered with the City of San Diego to ensure compliance with local lobbying laws.

*Material* means having significant importance. Factors that may be considered in determining materiality are: 1) significance of dollar amounts; 2) significance of percentages; 3) importance of item to purposes of State or local law; 4) frequency of occurrence; and 5) nature of transaction. A consideration in determining the materiality of errors in situations involving other than dollar amounts is whether the item or party can reasonably be identified. Parties that should be identifiable in the filings include the filers, employees, payees, subvendors, contributors, guarantors, *committees*, and beneficiaries.

*Post audit conference* means the meeting between the auditor and a representative of the

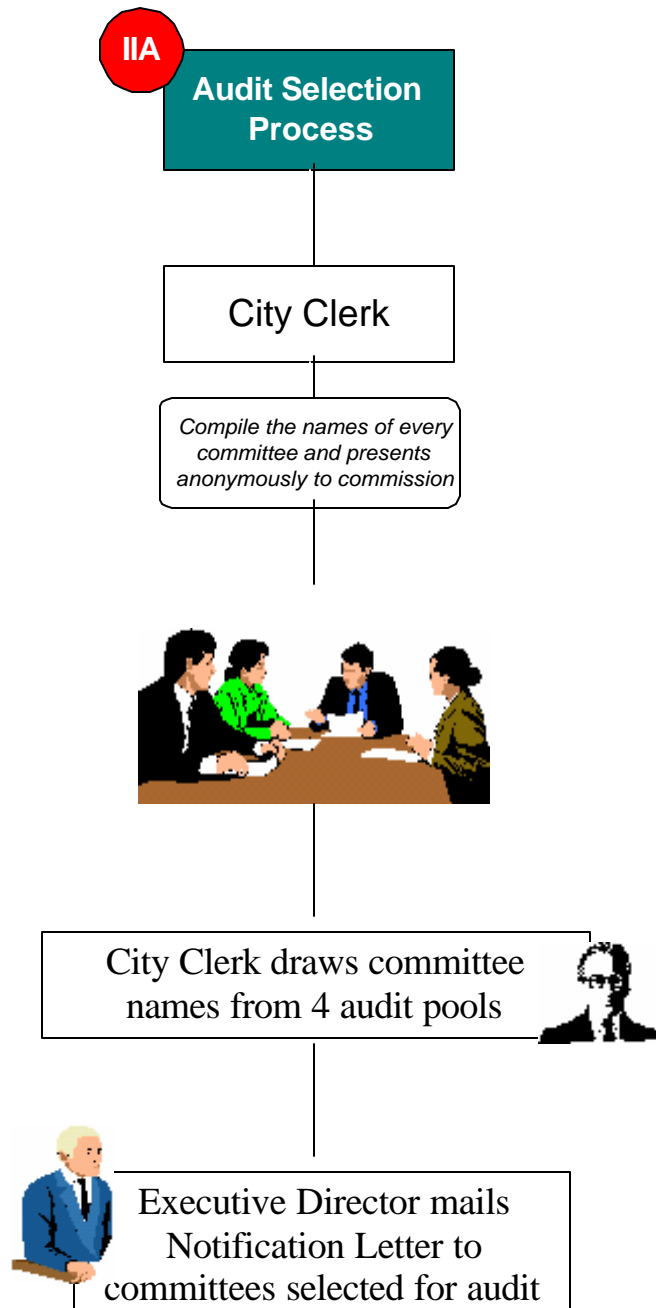


*committee* selected for the audit, held after the completion of the audit testing, and after the *committee* has had a reasonable opportunity to review the *draft audit report*.

*Preliminary audit tests* means a review of the *committee*'s campaign statements to determine whether the *committee* submitted the required filings and whether such filings contained all of the required information.

*Sampling* means selecting pieces of data that are extrapolated to make conclusions regarding the entirety of data that is the subject of the audit.

## II. AUDIT SELECTION PROCESS



The *Commission* has established guidelines regarding the selection for audit of *candidate committees* and *ballot measure committees*. Staff shall provide notice to *committees* whenever the *Commission* calendars the item of audit selection for consideration. The *Commission* shall also notify the *committees* that have been selected for audit.

In addition to the *committees* chosen in the random selection process, the *Commission* may audit *committees* as a result of filing irregularities identified by *City Clerk* staff.

## A. Campaign Audits

During every odd numbered year, the *Commission* shall schedule a random drawing of *committee* names at a meeting open to the public. This meeting shall take place prior to April 1 unless the *Commission* has good cause for scheduling the meeting on a later date.

Prior to the date of the random drawing, the *City Clerk* shall compile the names of (1) every *candidate committee* that supported or opposed a candidate who sought elective City office at an regular or special election held within the previous two calendar years; and (2) every *ballot measure committee* that filed a campaign statement with the *City Clerk* during the previous two calendar years. The names compiled shall be categorized by the following four criteria: (1) whether it is a candidate-controlled *committee*; (2) whether it is a *committee* other than candidate-controlled *committee*; (3) whether its financial activity was \$75,000 or greater; and, (4) whether its financial activity was between \$10,000 and \$74,999. A *committee* with less than \$10,000 in financial activity shall not be audited. The level of financial activity shall be based solely as follows:

- *Candidate committees*: the total of all monetary and non-monetary contributions and loans received by that *committee* since the last election for that office.
- *Ballot measure committees*: the total of all monetary and non-monetary contributions and loans received by that *committee* since the measure was approved for placement on the ballot.

Each *committee* potentially subject to an audit shall fall into one of the four audit pools depicted on the chart shown below.

### FOUR SEPARATE AUDIT POOLS

	Candidate Controlled Committees	Committees other than Candidate Controlled
Level of Financial Activity		
\$75,000 and greater	# TBD	# TBD
\$10,000 - 74,999	# TBD	# TBD

At the meeting in which the random drawing is conducted, the *City Clerk* shall present a list of the names of the *committees* subject to the random drawing. The *City Clerk* shall print the name of each *committee* on a separate piece of paper and place each *committee* name in its respective pool. Each piece of paper shall be indistinguishable from every other piece of paper except for the name of the *committee*.

Prior to the random drawing, the *Commission* shall determine whether any *committee* on the list is the subject of a pending enforcement action by the *Commission* and consider whether such *committee* should be subject to the audit selection process. The *Commission* may, subject to its discretion, instruct the *City Clerk* to refrain from placing into a pool the name of any *committee* that meets all of these criteria: (a) the enforcement action is based, in whole or in part, on an alleged violation of the City's Election Campaign Control Ordinance; (b) a formal investigation has been approved by the *Commission* with regard to the alleged violation; and (c) an audit of the *committee* would likely require duplicative efforts of *Commission* staff or otherwise result in an inefficient use of *Commission* resources.

At the time of the random drawing, the *Commission* shall determine, by majority vote, the number of *committee* audits to conduct during that calendar year, and the number of *committees* to be selected from each audit pool. The *Commission* shall conduct a maximum of four committee audits for the 2002 election cycle – one from each pool – and shall return to the City Council in future years with a proposal for the appropriate number of audits. Once this determination has been made, the *City Clerk* shall draw the *committee* names from the audit pools in a manner that ensures that the selections are made on a purely random basis.

## **B. Lobbyist Audits**

The *City Clerk* will conduct reviews of Lobbyist Registration and Quarterly Reports for compliance with the reporting requirements set forth in Chapter 2, Article 7, Division 40 of the San Diego Municipal Code [SDMC], entitled “Municipal Lobbying.” Deficiencies noted by the *City Clerk* may be referred to the *Commission* for possible investigation as a complaint.

The *Commission* will review and monitor *lobbyist* financial activity twice a year to ensure that *lobbyists* properly report activity expenditures on their Quarterly Reports and to ensure that individuals meeting with or providing gifts to *high level filers* are registered as *lobbyists* if they meet the threshold determination defined in SDMC section 27.4005. Any irregularities noted shall be referred to the *Commission* for possible investigation as a complaint. The objectives and procedures for this review are contained in the Lobbyist Audit Template under section V.

## **C. Conflict of Interest Forms**

The *Commission* will not conduct audits of Statement of Economic Interest forms filed by City Officials or candidates for elected office. The *City Clerk* will review these statements. Irregularities noted by the *City Clerk* may be referred to the *Commission* for possible investigation as a complaint. As part of the review of *lobbyist* activity expenses, the *Commission*

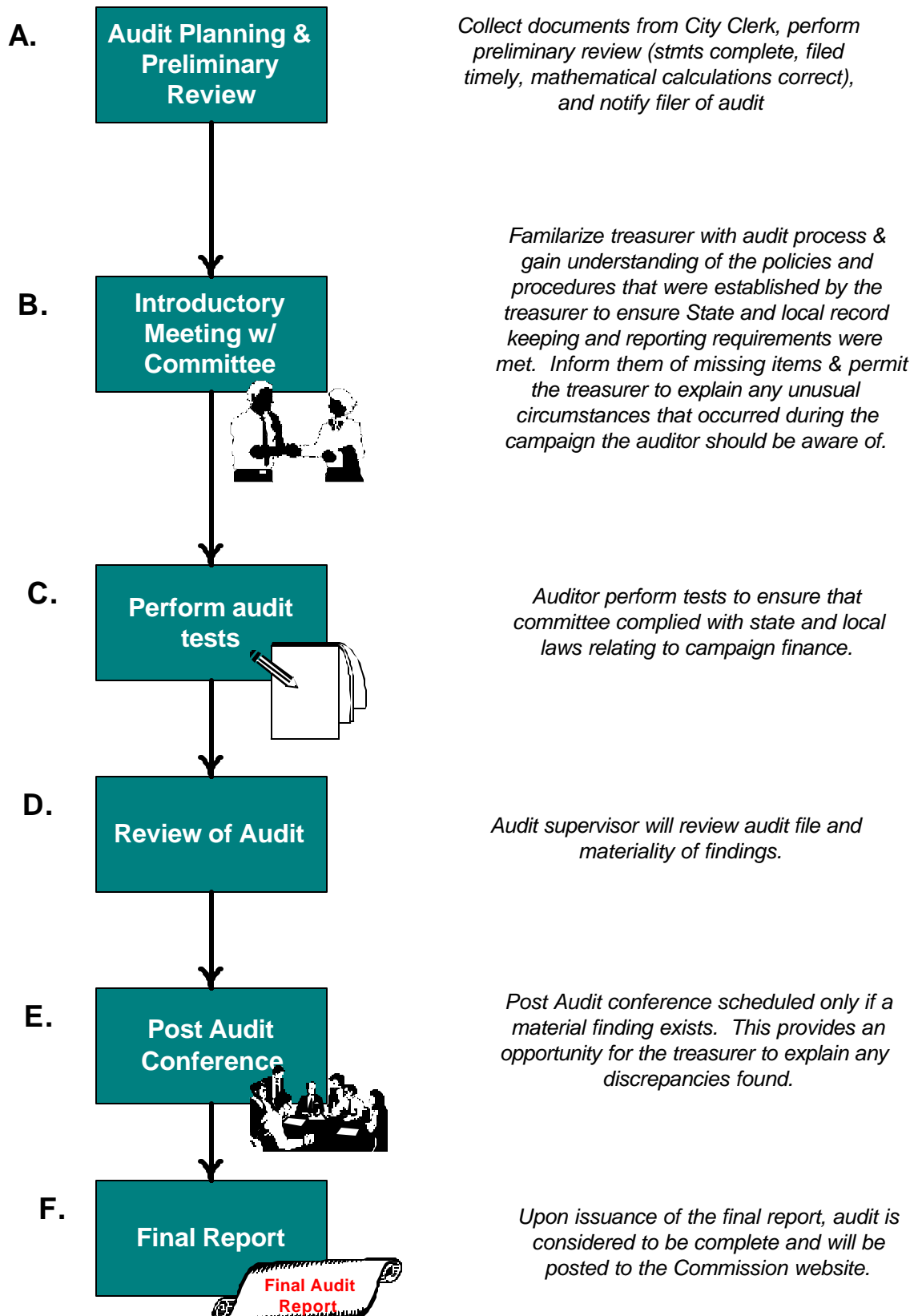
will review and monitor Schedule E - Income-Gifts to ensure that activity reported by a *high level filer* on Schedule E and received by a *lobbyist* was included on the Lobbyist Quarterly Report. The objectives and methodology for this review are contained in the Lobbyist Templates in section V.



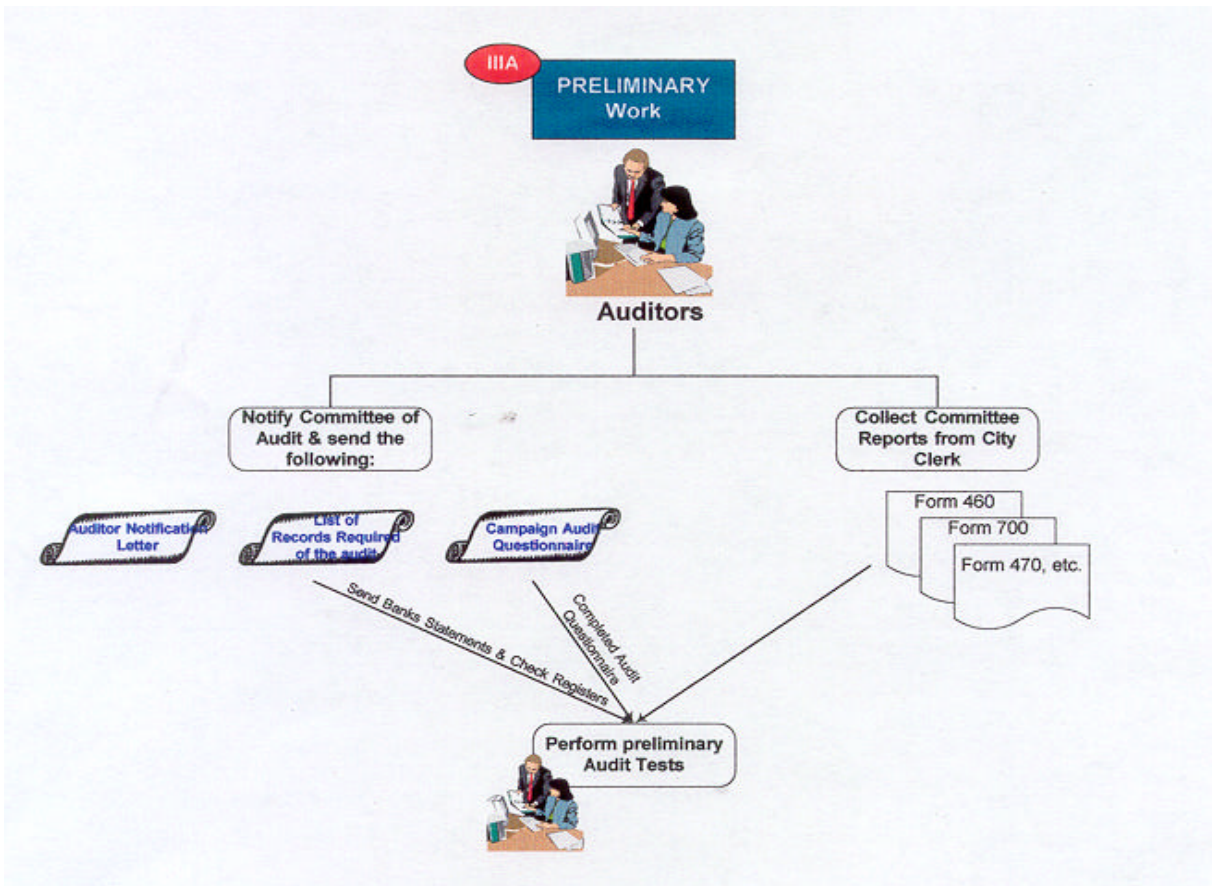
#### **D. Commission Notification**

The *Commission* shall send a *Commission notification letter* to each *committee* selected for audit. The *Commission notification letter* shall be sent without undue delay following the selection process described above in sections A and B. The *Commission notification letter* shall alert the *committee* of imminent contact by the auditor selected to conduct the audit.

### III. AUDIT PROCESS AND PROCEDURES



## A. Preliminary Work



The auditor shall make all reasonable efforts to minimize the time, effort, and expense required of the *committee* in complying with these audit procedures. In the event that the *committee* has been selected for an audit by the California Fair Political Practices Commission [FPPC] during the same calendar year, the auditor shall audit the *committee* chosen during its random drawing based only on those local regulations that are not part of the FPPC's regulations.

The auditor should attempt to complete preliminary work prior to the initial interview or examination of the filer's records. The preliminary work includes:

### 1. Preparation and Review of Audit File

- Audit file:

To prepare the *audit file*, the auditor should make copies of all relevant documents, which generally include the *committee's* campaign statements and reports, correspondence, documents submitted by the candidate regarding his/her candidacy, filings required under local law, previous audit reports, if any. Documents produced by the auditor and correspondence relating to the audit will be placed in the *audit file* with the above-referenced documents. See Appendix B for examples of documents that may be obtained from the City Clerk's office.

The auditor should review the *audit file* to determine whether there are missing statements, reports, or other filings. (For missing documents, the auditor should research the *Commission* files again - or the files of the *City Clerk*. Thereafter, if documents are still missing, the auditor should make note of this fact and discuss it with the *committee* prior to or at the *initial meeting*.)

- Analytical Review: Perform an analytical review of the statements and reports by reviewing the contents for: (1) completeness; (2) mathematical accuracy; and (3) consistency.
- Audit Period: Determine the *audit period*. Government Code Section 90002(c) provides the following guidelines for determining the *audit period*:
  - ✓ Audits of *candidate committees* and *ballot measure committees* cannot begin until after the last date for filing the first report/statement following the election(s) for the office for which the candidate ran, or following the election at which the measure was adopted or defeated.
  - ✓ Audits of *candidate committees* may cover all reports/statements filed since the last election for that office.
  - ✓ Audits of *ballot measure committees* may cover all reports/statements from the beginning date of the first report/statement filed in connection with the measure.

In accordance with the above-referenced guidelines, the following are some items to be considered in determining the *audit period*: 1) date the *committee* was formed; 2) dates covered by the last audit performed on the *committee*; 3) date the Intention to Solicit/Accept Contributions was filed; and 4) date the Statement of Organization was filed.

## 2. Contacting the Committee and Scheduling the Initial Meeting

The auditor should send an *auditor notification letter* to the treasurer and the *committee* to schedule the *initial meeting* with a representative(s) (usually the treasurer or candidate). (See Appendix C for an Auditor Notification Letter template.) With the *auditor notification letter*, the auditor should enclose: (1) a list of the records that are required for audit (See Appendix D for examples); and (2) a *campaign audit questionnaire* (as substantially set forth in Appendix E). The *auditor notification letter* should tell the *committee* to complete the *audit questionnaire* and return it to the auditor. In the case of a campaign related audit, the *audit questionnaire* should be returned with a copy of the *committee's* check register and bank statements, prior to the *initial meeting* but no later than when the audit testing begins. By obtaining the check register and bank statements prior to the *initial meeting*, the auditor will be able to review the *bank reconciliation* prior to the commencement of audit testing. If a *committee* has not conducted monthly *bank reconciliations*, the auditor should complete the *bank reconciliation*.

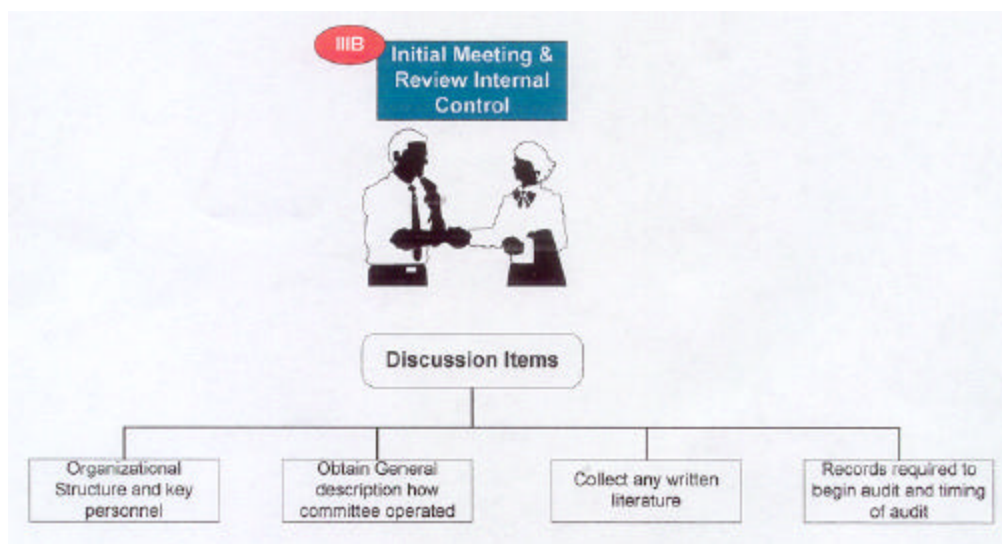
### 3. Performing the Bank Reconciliation and Preliminary Audit Tests

By reviewing or completing the *bank reconciliation* prior to audit testing, the auditor will be able to identify discrepancies and determine which periods/transactions to audit. Amended campaign statements should not be used when reviewing the *bank reconciliation* because most likely the *committee* did not rely on the amended information when completing its *bank reconciliation*.

Prior to obtaining and reviewing the *committee's* records, the auditor should perform the applicable preliminary testing. *Preliminary audit tests* may include a review of the *committee's* campaign statements to determine whether the *committee*:

- submitted the required filings by the prescribed deadlines
- filed statements and reports for the proper reporting periods
- provided the required contributor information (*campaign audits* only)
- abided by the contribution limits (*campaign audits* only)
- provided cumulative contribution amounts (*campaign audits* only)
- provided expenditure descriptions (*campaign audits* only)
- provided vendor information (*campaign audits* only)
- reported subvendor information (*campaign audits* only)

### B. Conducting the Initial Meeting and Evaluating Internal Control



## 1. Initial Meeting

At the *initial meeting*, the auditor should provide an overview of the audit process to the *committee* and answer any questions its representatives may have. The auditor should ask questions regarding the policies and procedures under which the *committee* operated and request additional information if needed. The auditor should ask the representative(s) to clarify any discrepancies the auditor may have found during the preliminary review or to explain in detail the responses that were provided on the *campaign audit questionnaire*.

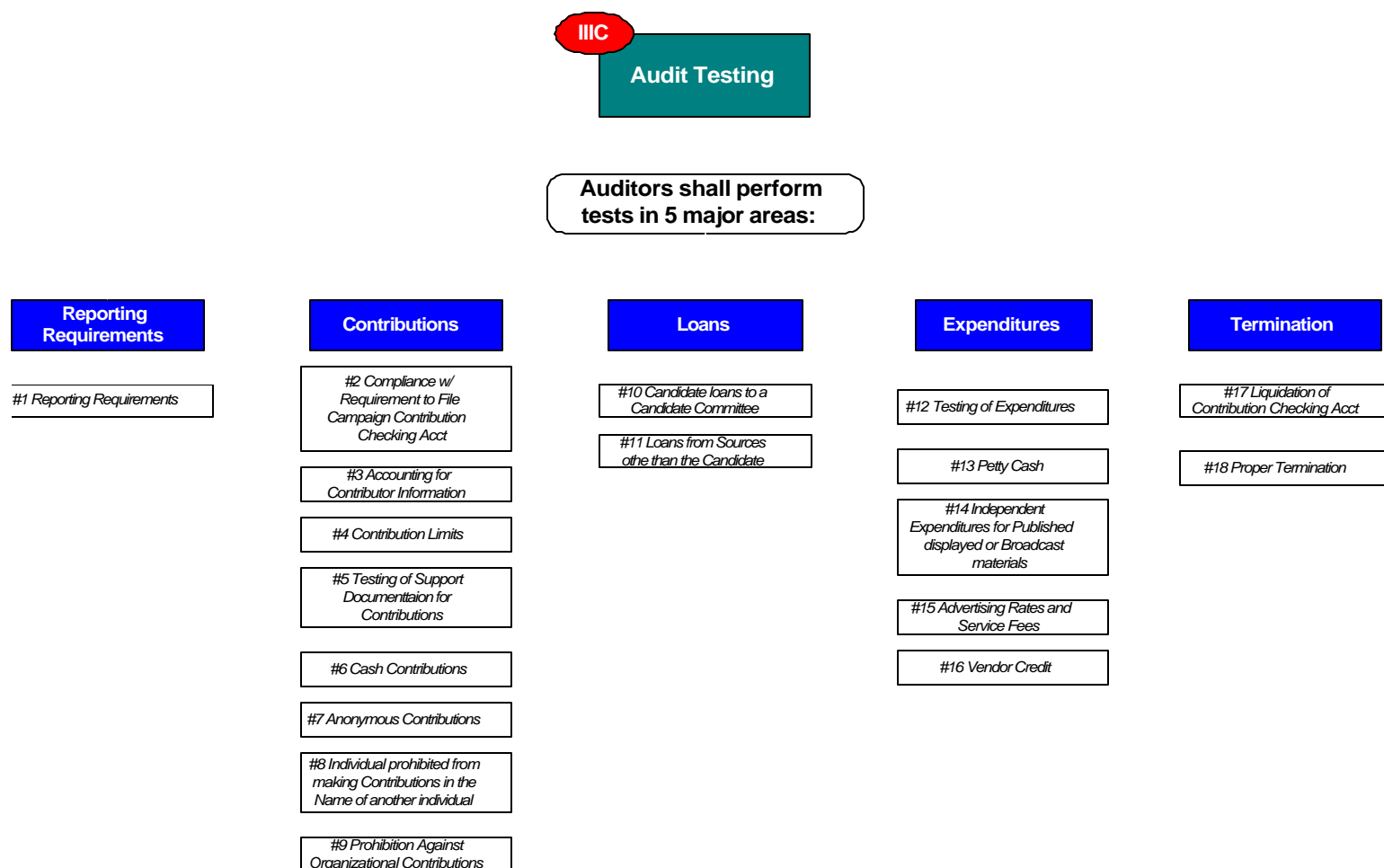
Topics for discussion include, but are not limited to:

- Organizational structure: review staffing functions and the division of responsibilities.
- Obtain organizational chart if available, or create one as part of the *audit workpapers* if it would be useful. Review the relationship between *committee* and candidate.
- A general description of how the *committee* operated. Ask for a general description of how funds were raised (e.g., luncheons, dinners, cocktail parties, neighborhood meetings, door-to-door solicitations, sales, etc.). Determine what type of advertising was used to promote the candidate/issue(s) (e.g., TV and radio spots, newspapers, literature, promotional gifts, etc.).
- Written literature: Ask for any brochures or similar literature used during the campaign.
- Records required to begin audit, which had been previously requested.
- Items disclosed by preliminary work that need to be discussed/clarified at this time.

## 2. Internal Control Review

The auditor should obtain detailed information about the accounting controls practiced by the *committee*. Obtaining such information will allow the auditor to evaluate the *committee's internal control* structure. *Internal control* is a coordinated system of procedures and techniques designed to safeguard an entity's assets, to ensure the accuracy of its accounting records, and to promote efficiency and adherence to prescribed policies. Note that the majority of campaign *committees* do not maintain a rigid system of *internal control*. Based on the completed *campaign audit questionnaire* and *initial meeting*, the auditor can evaluate the extent to which records are reliable. Factors affecting this evaluation include additional interviews, the general condition of the records, the results of the *bank reconciliation*, and results of an initial sample. The auditor must document the study and evaluation of *internal control*. Examples of criteria to be used for evaluating *internal control* are set forth in Appendix F.

## C. Conducting the Audit Testing



### 1. Audit Test Templates

The auditor shall conduct campaign audit testing in accordance with the templates contained in sections IV. The templates contain a list of objectives that the auditor must test to determine compliance. The criteria and objective for each test is identified. The methodology outlined for each test represents general procedures and guidelines. Because each audit will be unique based on the level of *internal control* established by the *committee* and the specific actions taken by the *committee*, the methodology outlined in the audit tests should be considered the minimal procedures that the auditor must perform. See Appendix G for audit testing procedures that may be used for statistical sampling.

The templates may not contain an all-inclusive list of requirements with which *committees* must comply. The auditor should make necessary adjustments to audit testing for any additions or changes to the laws and regulations applicable to campaign finance matters.

Compliance testing will be performed to determine whether a *committee* complied with the specific requirements of local law. Substantive testing is used to test for the existence

of a transaction, proper record keeping, and accuracy in disclosure. It is possible to conduct one test while simultaneously conducting part or all of another test.

## 2. Location of Audit Testing

The review of the records can be performed at the auditor's place of work or the location where the records are maintained. Once the auditor has access to the records, he/she can conduct the necessary testing. The records should include statements and reports that were filed by the *committee* and supporting documentation regarding transactions.

## 3. Audit Workpapers

The auditor must document in the *audit workpapers* all the tests conducted. The *audit workpapers* should also contain sufficient documentation regarding findings and documentation of requests for additional records or explanations provided by the *committee*. Documentation includes:

- A written record of relevant facts, figures and sources of information
- Photocopies of source documents when appropriate

The objectives, criteria and methodology used for each audit test as well as the auditor's conclusions based on the findings of the testing performed.

## D. Review of Audit

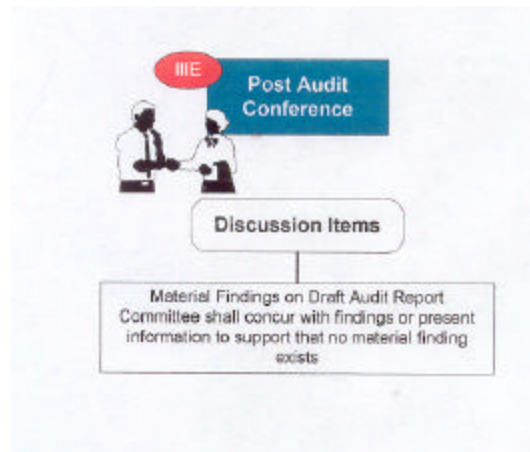
After the auditor has completed all audit testing, documented the results of all audit tests in the audit workpapers, and completed the *draft audit report*, the audit supervisor shall review the *draft audit report, audit file, and audit workpapers* for:

1. Depth, scope and adequacy of content and procedures
2. Application of written policy and procedures
3. Adequacy of presentation
4. Documentation of exceptions
5. All *material* findings to ensure that findings discussed in the *audit workpapers* are included in the audit report

The supervisor will review the materiality of all findings. If the supervisor disagrees with the auditor's determination of materiality, both the auditor and supervisor shall review the circumstances again and reconsider the materiality conclusion. A determination shall be made regarding whether to amend the *draft audit report* prior to the scheduling of the *post-audit conference*.



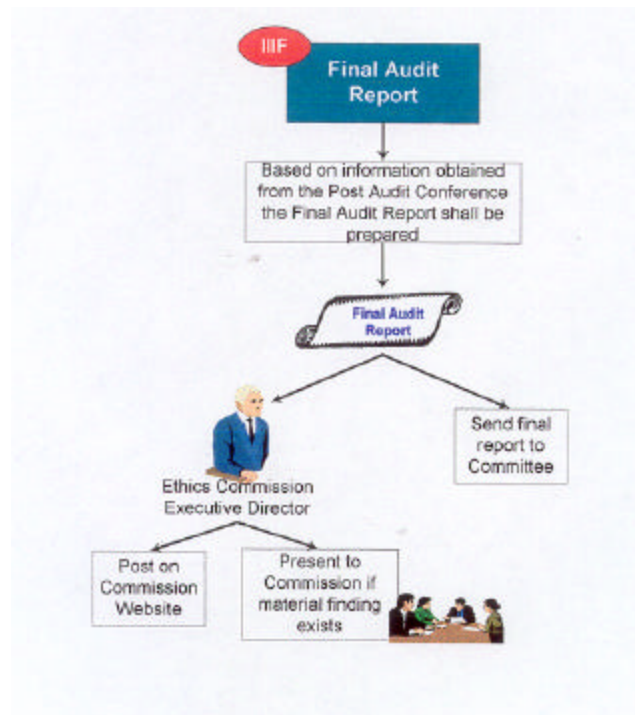
## E. Post-Audit Conference



A *post-audit conference* will be conducted at the completion of the audit testing, and after the *committee* has had a reasonable opportunity to review the *draft audit report*. The purpose of the *post-audit conference* is to discuss audit findings with the *committee*. In discussing the audit findings, the auditor should also discuss the positive aspects of the *committee's* records. Each finding should be fully explained. The *committee* may provide comments and explanations regarding the *material* findings.

The auditor should inform the *committee* that a *final audit report* will be forwarded to the *Commission* and, in cases of violation of law, to the appropriate enforcement agency. The auditor should also inform the *committee* that the audit is subject to review.

## F. Audit Reports



Audit reports are formal narrative documents based on the audit testing that was performed. These reports include a description of the *committee's* background information, the authority for the audit, the scope of the audit, and a summary of the results of the audit as expressed through written findings and determinations. If the audit produces no findings of a violation or produces only findings of a violation that are not *material*, the auditor shall prepare a *final audit report* and submit it to the *Commission*.

Audit reports that contain *material* findings shall be provided to the *committee*, in the form of a *draft audit report*, for comment. The *draft audit report* shall be sent to the *committee* no later than two weeks prior to the *post-audit conference*. If the *committee* provides additional documentation or a written explanation that may affect the materiality of a finding, the auditor shall review such information, and may reconsider the findings. After the *committee* has had an opportunity to comment on any *material* findings, the auditor shall prepare a *final audit report* and submit it to the *Commission*. The auditor should, in the *final audit report*, note any explanations and arguments raised by the *committee*. See Appendix H for a *final audit report* template.

The audit is concluded once the *final audit report* has been delivered to the *Commission*. All *final audit reports* shall be sent to the *committee* and posted to the *Commission's* website, and shall be made available for public inspection at the *Commission* offices.

If the *final audit report* contains *material* findings, the *Commission's* Executive Director shall present the report at a closed session meeting of the *Commission*. At this meeting, the *Commission* shall vote on whether the *material* findings contained in the *final audit report* warrant the initiation of a complaint. The *Commission's* consideration of the material findings shall be conducted in a manner essentially identical to its handling of a complaint that has been processed through the Preliminary Review stage and become subject to the *Commission* determination stage set forth in section 26.0423 of the San Diego Municipal Code. The *Commission* may instruct the *Executive Director* to either initiate a formal investigation or prepare a Draft Administrative Complaint and Probable Cause Report against the *committee* that is the subject of the audit.